Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	CC Docket No. 96-5
1995 Annual Access Tariffs	)	
GTE Telephone Operating Companies		Transmittal No. 963
GTE System Telephone Companies	)	Transmittal No. 146

VERIZON COMMENTS

The Commission should terminate its investigation into GTE's 1995 Annual Access filing because the designated issues have become moot. The parties to the proceeding investigating GTE's 1995 Annual Access filing each supports the of U S West Communications, Inc. **("U** S West") methodology for calculating exogenous cost adjustments to their PCIs for the sale of local exchanges. And since early 1996, each of the parties, including AT&T, has used the **U** S West methodology when making exogenous cost adjustments to their PCIs for the sale of local exchanges. Although there was some dispute at the time as to whether carriers should make ***upward*** adjustments to their PCIs when selling low cost exchanges, as GTE and US West explained then, just as the Commission recognized that downward adjustments are appropriate when carriers sell above-average cost exchanges, in a price cap regime, upward adjustments are appropriate when carriers sell below-average cost exchanges. No party seriously disputes this point now.

I. Parties to the 1995 Annual Access Filing Investigation Agree the U S West Methodology is an Appropriate Methodology for Calculating Exogenous Cost Adjustments for the Sales of Local Exchanges.

The Commission has asked parties to comment on "how carriers have made exogenous cost adjustments to their PCIs for the sale of local exchanges that occurred subsequent to 1995, and whether a dispute still exists over the appropriate methodology that should be used."[1]

In its Order Designating Issues for Investigation regarding GTE's 1995 Annual Access filing, the Commission was concerned primarily with the appropriate methodology carriers should use when calculating exogenous costs associated with the sale of telephone exchanges[2]. Prior to 1995, the Commission's rules with respect to the treatment of exogenous costs for sales of local exchanges were unsettled; thus, there were a variety of methods being used to calculate exogenous costs associated the sale of exchanges.[3] This issue is now moot because the parties to GTE's 1995 Annual Access

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1 *See Parties Asked to Refresh Record Regarding Order Designating Issues for Investigation Regarding GTE Sale of Several Local Exchange Properties,* FCC Public Notice, DA 07-1242 (rel. March 12, 2007)("Public Notice") at 1.

2 *1995 Annual Access Tariffs, GTE Telephone Operating Companies, GTE System Telephone Operating Companies,* Order Designating Issues for Investigation, CC Docket No. 96-5, Transmittal Nos. 963, 146 (CCB rel. Jan. 23, 1996)("Designation Order")

3 While U S West used a methodology that sought to identify specifically costs from the exchanges being sold and attribute them directly to those exchanges, GTE's methodology used the percentage of revenues from the exchanges being sold as a proxy to estimate the costs attributable to the exchanges being sold, adjusting its PCIs to reflect the fact that it would no longer own or receive revenues from sold exchanges' assets. Although GTE subsequently adopted the U S West methodology, GTE's use of revenues as a proxy for costs and its adjustment of various price cap indices is not unique. The Commission has used a similar approach where services have been removed from price cap regulation to reflect the transfer of assets to a separate affiliate. For example, when the Commission conditioned its approval of the Bell Atlantic-GTE merger on Bell Atlantic transferring its broadband assets to a separate affiliate, relative revenues were used to adjust "R values" to reflect the fact that the ILEC no longer assumed the costs and revenues associated with the service and its underlying assets. *See* December 15, 2000 Letter from Kenneth W. Rust to Magalie Roman Salas, filed electronically

Filing Investigation agree that the U S West methodology is the appropriate methodology for calculating exogenous costs attributable to the sale of local telephone exchanges. This method has been used since 1996.

In its Direct Case, filed in response to the Designation Order, GTE agreed that prospectively "it would be more appropriate to identify the exogenous costs attributable to the sale of exchanges using the method proposed by U S West."[4] Likewise, in its Comments on GTE's direct case, AT&T stated that it "supports GTE's decision to identify the exogenous costs attributable to the sale of high cost telephone exchanges using the method proposed by U S West."[5] In its Rebuttal Comments, AT&T again urged the Commission to "accept GTE's use of the U S West methodology ...."[6]

The U S West methodology for calculating exogenous costs associated with the sales of local exchanges was accepted industry practice by the time GTE filed its 1996 Annual Access filing. In this filing, GTE again included exogenous cost adjustments relating to the sale of local telephone exchanges, this time for local exchanges in Texas that had not closed in time for the 1995 filing but were complete for the 1996 Annual Access filing. In that filing, GTE used the U S West methodology to calculate those exogenous costs and adjust its PCIs. AT&T again filed a petition but did not object to

via ETFS (removing services from price cap and transferring to VADI). Similarly, revenues were used to adjust "R Values" when DSL services were no longer provided as a common carrier offering in accordance with the ***Wireline Broadband Internet Access Order.*** See August 15,2006 Letter from Amy Kavelman to Marlene H. Dortch, filed electronically via ETFS (removing DSL services from price caps)

[4] ***See*** GTE Direct Case, CC Docket 96-5, Transmittal Nos. 963, 146 (Feb. 20, 1996)("GTE Direct Case") at 4.

[5] ***See*** AT&T Comments, CC Docket 96-5, Transmittal Nos. 963, 146 (Mar. 5, 1996)("AT&T Comments") at 1, 4.

[6] ***See*** AT&T Rebuttal Comments, CC Docket 96-5, Transmittal Nos. 963, 146 (Mar. 19, 1996)("AT&T Rebuttal Comments") at 4.

GTE's use of the U S West methodology to calculate exogenous costs associated with the sale of local exchanges in Texas.[7] Although AT&T also complained that GTE had not adjusted for sales in the Missouri, Oregon, and Washington exchanges that GTE had previously reversed, GTE noted that exchange sales had not occurred in those states for the period covered by GTE's 1996 Annual Filing.[8]

At least twice since then – in 1997, when GTE adjusted for the sale of local exchanges in Missouri, and in 1998, when GTE adjusted for the sale of local exchanges in Washington – GTE has calculated exogenous costs associated with the sale of local telephone exchanges using the U S West methodology, and no party has objected to the use of this methodology. *See* GTE 1997 Annual Access Filing (adjusting for sale of exchanges in Missouri); GTE 1998 Annual Access Filing (adjusting for the sale of local exchanges in Washington). Moreover, other carriers, including AT&T, have used the U S West methodology when calculating exogenous costs associated with the sale of exchanges. See Ameritech 1999 Annual Access Filing at Exhibit 5. Accordingly, there is no longer any dispute among the parties that the U S West methodology for calculating exogenous costs relating to the sale of local exchanges is an appropriate methodology.

III. The Commission Should Allow Exogenous Adjustments that Reflect Upward and Downward Cost Changes From Exchange Sales.

The Commission also seeks comment on whether carriers make upward as well as downward exogenous adjustments to their PCIs and any explanation as to why carriers would not make upward adjustments. Public Notice at 1. Although Verizon has not identified any sales of exchanges that resulted in upward adjustments to its PCIs since the

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[7] See AT&T Petition to Suspend and Investigate Transmittals No. 1026 and 178 (April 29, 1996)("AT&T Petition") at 20-21.

[8] See GTE Reply to AT&T Petition (May 13, 1996) at 5-6.

1995 and 1996 Annual Access Filings, as GTE and U S West explained in comments and reply comments filed in response to the Designation Order, upward adjustments are appropriate in cases where carriers sell exchanges that have costs that are below the carrier's average costs. As the Commission recognized in its ***First Report** and **Order,*** "sales or swaps of exchanges should result in an exogenous adjustment to the price cap carrier's PCI."[9] Because the Commission was concerned then with removing incentives for price cap LECs to "game the system" and realize "windfall profits" by selling high-cost exchanges, the Commission stated that the sales of high-cost exchanges should result in downward adjustments to a price cap LECs' PCIs. This "departure from the Commission's general standard for determining exogenous cost changes" the Commission explained was "necessary to maintain consistency with the concept of the price cap plan overall." ***Id.*** The Commission never addressed or discussed exogenous adjustments that would be appropriate when carriers sold low-cost exchanges. ***See*** Reply Comments of U S West at 3-4; ***see** also* Rebuttal of GTE at 2-3.[10]

Contrary to AT&T's claims at the time then, it is not "clear" that the Commission intended to limit exogenous adjustments from sales of exchanges to downward adjustments. Moreover, such a position would be contrary to the Commission's longstanding practice of considering exogenous factors that would result in both upward and downward exogenous cost adjustments as necessary to maintain price cap rates. As both GTE and U S West explained, limiting exogenous cost adjustments to only those sales of exchanges that produced a downward PCI adjustment would result in rates which

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[9] ***See Price** Cap **Performance Reviewfor Local Exchange Carriers,*** First Report and Order, FCC 95-132 (rel. April 7, 1995)("First Report and Order) ¶ 328.

[10] ***See*** CC docket 96-5, March 19, 1996.

were "unreasonably low," a result that also is contrary to the goals of price cap regulation. U S West Reply Comments at 5. To maintain consistency with the price cap plan overall, both upward and downward adjustments must be available.

In addition, restricting exogenous treatment to sales that produce only downward adjustments is contrary to the public interest in that it would discourage LECs from disposing of properties even in instances where the exchange might be of greater strategic value to or even more profitable for a potential buyer, and selling the exchange would increase the efficiencies of both the seller and the buyer. Rebuttal of GTE at 3; U **S** West Reply Comments at 5. Accordingly, to the extent the Commission issues a ruling in this matter, it should conclude that both downward and upward exogenous adjustments are appropriate when considering the effect of a sale of exchange on a carrier's PCI.

IV. Conclusion

For the reasons stated above, the Commission should terminate its investigation into GTE's 1995 Annual Access Filing.

Respectfully submitted,

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